



PO Box 987 Pakenham Vic 3810

P | 1800 932 394

F | 03 8738 1577

E | admin@eziway.net.au

Submission in Response to Proposed Changes to Limiting Fringe Benefits Tax Concessions on Salary Packaged Entertainment Benefits

For the attention of:
The General Manager
Law Design Practice
The Treasury
Langton Crescent
PARKES ACT 2600

Summary

The highly complex Australian taxation system levies over 100 different taxes within a sluggish and costly compliance environment.

Within this intricate taxation structure, successive governments have provided a degree of support to NFPs via tax concessions. These concessions are a valuable tool in supporting NFPs to attract and retain staff, reduce operating costs and deliver community support. They allow organisations to extend certain salary sacrifice benefits to employees, which serve to partly redress the below market wages available within the sector. Such salary packaging benefits are shown to be powerful staff motivators.

In 2015, the federal government proposed fundamental changes to limit the use of salary packaged entertainment benefits. It is suggested generous NFP tax concessions are compromised by inequity, widespread rorting and inappropriate employee lifestyle subsidy. It is claimed the low wage earners tax concessions should primarily assist are excluded from benefiting and that high earners (particularly within the public health sector) are availing themselves of excessive benefit, resulting in great loss of taxation revenue.

A number of measures are proposed with an overall objective to “improve the integrity of the tax system”, by addressing entertainment salary packaging benefits and specifically:

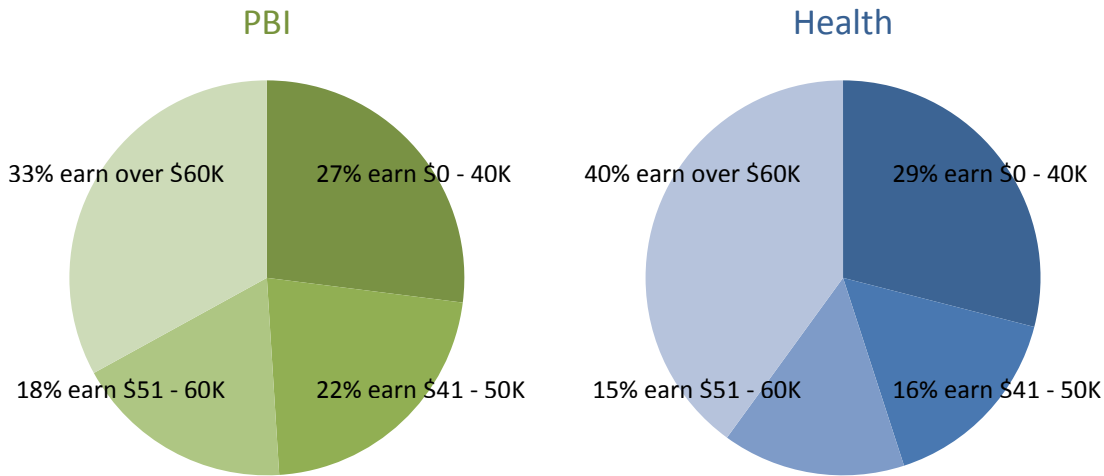
- Removing reporting exclusion,
- Removing elective valuation rules,
- Introducing an annual benefit cap.

As a remuneration industry provider, exclusively servicing FBT-exempt employers, eziway is in a unique position to know and share factual salary packaging data. Scrutiny of actual remuneration data collected over the 2014-2015 FBT year suggests disparate trends within the public health and charity sectors, providing good grounds for considering these service provider groups independently. Further, data analysis does not necessarily align with government assumptions in respect to benefit access, typical claim value and lost taxation revenue estimates.

eziway maintains the vast majority of concerns around provision salary packaging could be simply addressed by uplifting the annual benefit limit and introduction of an all-encompassing cap. We further content a genuine appetite for enhancing the integrity and equity of Australia’s taxation system should involve a program of broad PAYG reform.

Not for profit sector remuneration

eziway salary packaging data shows the majority of employees working within Australia’s not-for-profit sector earn less than \$60K annually. This can be specifically broken down as follows:



The bulk of not-for-profit employees are in no financial position to leverage unfair advantage from salary packaging benefits. However, they are more likely than employees earning \$60K or more (in any wage group) to access entertainment salary packaging benefits. This demonstrates the importance of benefit availability to low end wage earners.

Not all employees of FBT-exempt organisations qualify to participate in salary packaging programs. Many organisations are unable to support the extra administration burden of extending benefits to casual employees and, for any real wage advantage to be gained, employees need to earn a minimum gross wage of \$24K annually. By default, this flooring excludes the bulk of part time employees. For these reasons, eziway estimates up to 40% of not-for-profit sector employees are unable to access salary packaging.

Even within this context, eziway salary packaging data collected over the 2014-2015 FBT year reveals low end wage earners make up the highest proportion of entertainment benefit participants.

PBI	
Annual wage category	Claim proportion
\$0 – 40K	30%
\$41 – 50K	17%
\$51 – 60K	14%
all other groups	39%

Health	
Annual wage category	Claim proportion
\$0 – 40K	30%
\$41 – 50K	16%
\$51 – 60K	14%
all other groups	40%

Govt assumptions –v– eziway findings

Generous tax concession

Assumption

The government provides significant support to NFP sector through tax concessions that allow organisations to use salary packaging benefits as a staff incentive

Fact

According to the Australian Bureau of Statisticsⁱ in May 2015 Australia's average annual private sector wage is \$75.6K. eziway salary packaging data collected over the 2014-2015 FBT year shows 61% of PBI employees and 60% of public health employees earn less than \$60K.

To employees, the typical tax benefit of capped salary packaging is less than \$5K, making real not-for-profit wages more than \$10K below market.

Regulatory requirements impose a significant administration and compliance cost on employer organisations:

Workforce size	Annual administration	Yearly overhead
<1,000	406 hours	\$12,869
2,000	2,272 hours	\$72,043
3,000	2,640 hours	\$83,670

Inequity

Assumption

Salary packaging entertainment benefits unfairly advantage high income earners.

Fact

Not-for-profit sector data collected by eziway over the 2014-2015 FBT year shows high income earners access entertainment benefits least frequently than every other group.

PBI		Health	
Annual wage category	Claim proportion	Annual wage category	Claim proportion
\$90 – 100K	2%	\$90 – 1000K	3%
\$100K +	7%	\$100K +	10%

Rorting

Assumption

Widespread corruption exists leading to exorbitant and unfair claims.

Fact

Data collected by eziway over the 2014-2015 FBT year shows around 30% of employees access salary packaging entertainment benefits, with an average actual dollar values:

PBI		Health	
eziway Outsourcing Professionally administered salary packaging		eziway Licensing Self-administered salary packaging	
PBI average claim	Health average claim	PBI average claim	Health average claim
\$4,380	\$5,187	\$1,497	\$5,895

Inappropriate

Assumption

It is not fitting for the tax system to fund lifestyle benefits for employees.

Fact

All potential for rorting, inequity and benefit suitability could be resolved by increasing the annual limit to create one, all-encompassing capped threshold. This would also alleviate the costly and time-consuming administration burden borne by NFP organisations.

Removing reporting exclusion

A 2010 Productivity Commission report noted the “meal entertainment benefit is particularly inequitable, with greater benefits flowing to employees with higher salaries, and those who have greater financial freedom to spend their salaries on eligible items”.ⁱⁱ

This position is not borne out by salary packaging data, which clearly demonstrates wage earners in the under \$60K annual salary bracket submit significantly more entertainment claims than any other group. Far from the claims of excess, average claim values processed by eziway outsourced program administration are:

PBI			Health			
Annual wage category	Avge pre-tax annual claims	Avge net annual value	Annual wage category	Avge pre-tax value	Avge net value	Avge net annual value
\$0 – 40K	\$2,680	\$1,017	\$0 – 40K	30%	\$4,173	\$790
\$41 – 50K	\$3,251	\$1,235	\$41 – 50K	16%	\$4,466	\$1,383
\$51 – 60K	\$4,010	\$2,479	\$51 – 60K	14%	\$4,720	\$1,529

There are isolated cases of benefit exploitation, which rarely originate in PBI organisations, almost exclusively occurring in the public health sector, and biased towards self-administered programs.

The non-reportable nature of exempt benefits effectively constrains the availability of remuneration data. On the surface, there would appear to be no compelling reason for excluding this information from the taxation system.

Non-reporting of entertainment benefits offers not-for-profit organisations no particular advantage in recruitment competitiveness, overheads or service provision. However, the introduction of entertainment benefit reporting would be more productive as part of a broader tax reform strategy.

Removing elective valuation rules

Compliant benefit processing is a definite issue within the not-for-profit sector, particularly with in-house program administration, where there may not be the technology or expertise to handle claims within regulatory guidelines, or where there is potential for staff to be unduly influenced to process non-compliant claims.

Having transitioned over 200 organisations in 8 years, eziway has frequently observed and addressed non-compliance through outsourced service provision. This can be demonstrated by:

eziway Outsourcing			eziway Licensing		
Professionally administered salary packaging			In-house administered salary packaging		
Income group	Claim value	Average claim	Income group	Claim value	Average claim
\$100K+	>\$10K	\$18.1K	\$100K+	>\$10K	\$25.6K

This issue is closely linked to the scope of entertainment benefits and nature of event expenditure.

A choice of three different valuation methods is more involved than benefit access requires and demands highly specialised knowledge that is costly for employees to nurture and maintain in-house.

Having said that, standardising benefit valuation rules would be of higher value to the overall taxation system as part of broader reform, including revision to the classification of benefits and claim status.

Introduction of annual entertainment benefit cap

One of the main arguments in favour of salary packaging is the ability for health and charity organisations to remain competitive against private sector remuneration. With Australia's average annual wage now \$75.6K and, 70% of not-for-profit employees earning \$70K or less, the overwhelming majority of the sector is remunerated at below market wages.

Annual capped benefit limits partly off-set wages disparity but relying on grossed up values based on the FBT rate bears little resemblance to the real net wage value to employees:

Annual salary	\$0-40K	\$41-50	\$51-60
Portion of wage earners in PBI sector	30%	17%	14%
Salary Packaging benefit cap	\$15,900	\$15,900	\$15,900
Reportable Fringe Benefit value	\$31,177	\$31,177	\$31,177
Tax scale	19 / 32.5c	32.5c	32.5c
Maximum real wage value to employee	\$3,744	\$5,094	\$5,485

Annual salary	\$0-40K	\$41-50	\$51-60
Portion of wage earners in Health sector	29%	16%	15%
Salary Packaging benefit cap	\$9,010	\$9,010	\$9,010
Reportable Fringe Benefit value	\$17,667	\$17,667	\$17,667
Tax scale	19 / 32.5c	32.5c	32.5c
Maximum real wage value to employee	\$2,297	\$3,108	\$3,108

To the 60% of not-for-profit employees earning \$60K annually or less:

- The proposed grossed up value in real wages terms is valued no more than \$828, and
- The total of all salary packaging benefits available under this proposed new regime, in real wage value to employees, are valued no more than \$5,996.

Case for FBT Concessions

The federal government recognises the contribution of NFP sector to the Australian community via tax concessionsⁱⁱⁱ. This is consistent with general community expectations that services provided by not-for-profit organisations warrant some form of government assistance or subsidy. To some extent, government tax concessions are made available in lieu of funding.

In 2010, a Lateral Economics report^{iv} concluded “dividend from any wholesale removal of the concession would be meagre at best, and that quite possibly reform would lead to worse result”.

The currently available tax concessions allow FBT-exempt employers to:

- compete more equitably and draw skilled employees with more attractive real wages,
- reduce operating expenses through lower wage expenditure,
- free up valuable resources that can be redirected into service provision.

There is strong evidence that salary packaging benefits are very important to employee recruitment, engagement and retention for both charities and public health services.

Possible outcomes of change

Government has already taken significant steps to scale back not-for-profit support, creating funding uncertainty in the public health and PBI sector and asking organisations already under service provision duress to do more with less.

Funding pressure has already driven a large portion of sector employment into casual or part time work and a much higher level of tenure insecurity now exists within the sector. The addition of loss of benefits can only lead to lower levels of job satisfaction.

In its report, Lateral Economics included sector survey results that found just 18% of employees would remain working in the sector if significant changes were made to salary packaging benefits (FBT tax concessions).

Any fall in not-for-profit sector employee retention is likely to result in:

- Workers moving from public to private health or away from PBI employers,
- Loss of highly specialised skills within health, disability services, aged care and like services experiencing unprecedented and growing demand,
- Redirection of not-for-profit resources away from service delivery to wages and entitlements,
- Higher staff turnover resulting in amplified recruitment costs and lower financial efficiency,
- Diminishing volume and standard of services delivered.

Wages disincentive may also result in employee behaviour change, marked by scaling back work hours, finding other ways to avoid tax or leaving the sector entirely.

Conclusion

In its latest not-for-profit sector survey^v, Pro Bono Australia concludes:

“The operating environment for Australian Not for Profit organisations is volatile with fundamental changes to Federal Government regulation and policy and funding mechanisms at both Federal and State levels. These changes coincide with ever increasing volume of demand for services and increasing expectations in terms of access to and the quality of those services.”

Two vital factors are identified as having the most positive impact in the sector:

- Human Capital,
- Funding.

Protecting the investment in skills, experience and service delivery is paramount to avoiding momentous sector decline. This is an important consideration in the proposed changes to limiting fringe benefits tax concessions on salary packaged entertainment benefits. When assessing the measures suggested, it is vital we look beyond the sensational claims of unfair advantage that are simply not borne out in reality to the benefit and cost of their implementation.

The simple fact is, those who stand to be disadvantaged by these changes are the very individuals that tax concessions set out to benefit most. The huge majority of low end wage earners employed by charities and public health service providers.

eziway is supportive of an objective that produces a more fair and equitable taxation system. Were this to include new salary packaging benefit capping and reporting requirements, a gross-up of exempt benefits amounts split between public hospitals and charities would be a fairer option.

However, we believe no steps can be effective in isolation and such wholesale changes would be more appropriately bundled with general tax reform. In this way, Not for Profit sector concessions would be properly considered in the context of an overall tax package.

Most particularly, extensive FBT system changes could lift the compliance cost burden and help the Not for Profit sector to channel more resources into their organisational purpose.

Enquiries

Paul Gozzo

Managing Director
eziway Group

e | paul@eziway.net.au

m | 0433 330 011

p | 03 8768 5777

w | www.eziway.net.au

ⁱ Australian Bureau of Statistics, Average Weekly Earnings, Australia, May 2015, catalogue 6302.0

ⁱⁱ Australian Government Productivity Commission, Contribution of the Not-for-Profit Sector, January 2010

ⁱⁱⁱ Australian Government, Re:think Better tax, Better Australia Discussion Paper, 2015

^{iv} Lateral Economics, The case for retaining the FBT concession for not for profit Hospitals/Aged Care and Public Benevolent Institutions (Charities), 2010

^v Pro Bono Australia, State of the Not for Profit Sector Survey, 2014